

**BEFORE THE NEBRASKA PUBLIC SERVICE COMMISSION**

In the Matter of the Nebraska Public Service Commission, on its own motion, to make adjustments to the universal service fund mechanism established in NUSF-26.

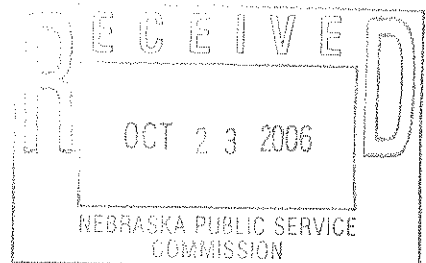
Application No. NUSF-50

In the Matter of the Commission, on its own motion, seeking to determine the level of the fund necessary to carry out the Nebraska Telecommunications Fund Act.

Application No. NUSF-4

**REPLY TESTIMONY OF MARK D. HARPER  
ON BEHALF OF  
UNITED TELEPHONE OF THE WEST d/b/a EMBARQ**

October 23, 2006



1           **I.       INTRODUCTION**

2   **Q.     Please state your name, business address, employer, and position.**

3   A.     My name is Mark D. Harper. I am employed by Embark Corporation as Director  
4           – State Regulatory in the Law and External Affairs Department. My business  
5           address is 5454 W. 110<sup>th</sup> Street, Overland Park, Kansas 66211.

6

7   **Q.     Are you the same Mark D. Harper who filed direct testimony in Application**  
8           **NUSF-50/4?**

9   A.     Yes, I am.

10

11   **Q.     What is the purpose of your reply testimony?**

12   A.     My reply testimony will respond to issues raised by other parties in their direct  
13           testimony regarding the Commission's proposed changes to the NUSF  
14           distribution mechanism and provide Embark's position in relation to those  
15           issues.

16

17           **II.     SUFFICIENCY OF FUND**

18   **Q.     Several parties testified that the Commission's proposed changes threaten the**  
19           **predictability and sufficiency of the NUSF. Do you agree?**

1 A. Yes, I do. The proposed changes result in a 34 percent reduction in high cost  
2 distributions from the fund. Based on the Commission's proposal several  
3 carriers will lose all NUSF high cost support as a result of these changes while  
4 others will lose more than 50 percent of their support.

5  
6 One of the goals of the NUSF was to "encourage the development and  
7 maintenance of the telecommunications infrastructure and encourage investment  
8 and the deployment of new technologies."<sup>1</sup> While I am not a lawyer, Nebraska  
9 law clearly states in lay terms that, "it is the policy of the state to preserve and  
10 advance universal service based on the following principles: (2) Access to  
11 advanced telecommunications and information services should be provided in  
12 all regions of the state..." For the most part the Commission is succeeding in  
13 achieving this goal. Embarq has invested heavily in its serving territory, with  
14 broadband capability now available in all of its exchanges and the recent  
15 deployment of packet switching technology in Scottsbluff. These investments  
16 have brought many advanced services to Nebraskans in Embarq's service  
17 territory. Under the Commission's proposal, however, Embarq stands to lose  
18 almost 40 percent of its NUSF high cost support for its rural customers. If the  
19 support for these high cost rural areas is lost or dramatically reduced, the further

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<sup>1</sup> *In the Matter of the Nebraska Public Service Commission, on its own Motion, seeking to establish a long-term universal service funding mechanism*, Application No. NUSF-26, Progression Order #2, issued August 27, 2002, paragraph 29.

1 deployment of additional advanced services to Embark's customers will slow  
2 considerably. The proposed changes would make the NUSF unpredictable and  
3 insufficient.

4  
5 **Q. Mr. Jeffrey Pursley of the Nebraska Telecommunications Infrastructure and**  
6 **Public Safety Department states that "[c]hanges to high cost support levels**  
7 **must occur in early 2007 in order to keep the fund solvent" on Page 3 of his**  
8 **direct testimony. Do you agree that reducing high cost support is the only**  
9 **option available to the Commission for ensuring fund solvency?**

10 **A.** No, as stated in my direct testimony and agreed to by several other parties, the  
11 Commission can and should raise the surcharge to the level necessary to at least  
12 continue funding high cost rural areas at the level ordered in NUSF-26. The  
13 Commission's proposal only focuses on the issues of the solvency of the NUSF at  
14 the reduced surcharge level. Neither the Commission's proposal nor any of the  
15 responding parties' testimony provides public policy support for why the  
16 proposed reduced funding meets the requirements of federal or state statutes, or  
17 why the existing funding mechanism established in NUSF-26 is no longer  
18 consistent with those same statutes.

1    **Q.    Mr. David Ruhland, on behalf of Frontier,<sup>2</sup> recommends that the NUSF**  
2       **surcharge not be raised, do you agree?**

3    **A.    No. Mr. Ruhland, at Page 2 of his testimony, expresses concern that raising the**  
4       **surcharge “sends a confusing message to Nebraska consumers.” Dr. Staihr**  
5       **explains in his reply testimony why raising the surcharge level is appropriate.**  
6       **Mr. Ruhland, at page 3, goes on to conclude that “NUSF support cannot be relied**  
7       **upon as a long-term source of funding to support major infrastructure**  
8       **upgrades.” He then proposes that companies should be permitted “to transition**  
9       **to recovery of a greater proportion of costs directly through end-user service**  
10      **rates.”**

11  
12   **Q.    Is passing the costs of supporting high cost areas directly to those customers a**  
13      **good public policy decision?**

14      No. Mr. Ruhland’s assessment that the NUSF has become unpredictable may be  
15      accurate, particularly in light of the current proposal before the Commission, but  
16      the cure should not be worse than the disease. Changes to the NUSF should not  
17      abandon the social goal of reasonable, comparable, and affordable rates in all  
18      areas, as the current proposal does. Instead, changes to the NUSF should

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<sup>2</sup> Citizens Telecommunications Company of Nebraska d/b/a Frontier Communications of America (“Frontier”).

1 represent a recommitment to those goals and the adequate funding of the high  
2 cost areas in Nebraska.

3  
4 Forcing service providers to increase prices inappropriately shifts the costs of  
5 serving high cost areas directly to the customers who live in them. This is  
6 entirely contrary to the policy behind universal service:

7 Consumers in all regions of the state, including low-income consumers  
8 and those in rural and high-cost areas, should have access to  
9 telecommunications and information services, including interexchange  
10 services and advanced telecommunications and information services,  
11 that are reasonably comparable to those services provided in urban  
12 areas and that are available at rates that are reasonably comparable to  
13 rates charged for similar services in urban areas. Neb. Rev. Stat. § 86-  
14 323(3).

15 Moreover, placing costs directly on the customers in high cost areas is simply not  
16 feasible for Embarq. If the support for these customers were removed the  
17 Embarq customer local service rate in the supported areas would have to  
18 increase by more than \$45 per month.

19  
20 **Q. What is Frontier's solution to the problem of imposing unnecessarily high**  
21 **costs on customers who live in high cost areas?**

22 Frontier seems to be suggesting that the current support would be spread over  
23 all customers. On Page 3 of the testimony, Frontier proposes that "carriers be

1 allowed to adjust all residential customers rates based on one statewide  
2 residential benchmark.”

3  
4 **Q. Why is this suggestion a bad idea?**

5 This process would simply serve to move the industry back to the untenable  
6 position that caused the need for the NUSF. Universal service is in peril in a  
7 competitive environment when ILECs must rely on implicit subsidies embedded  
8 in rates to ensure that customer rates in high cost areas remain affordable. In  
9 other words, as Embarq loses customers in lower cost areas the support  
10 embedded in those lost revenues is no longer available to support the costs of  
11 serving customer in high cost areas. Embarq is losing customers across its  
12 Nebraska service areas to wireless carriers and in two exchanges is facing a  
13 facilities based competitor for both residence and business customers. Any  
14 significant rate increases in these areas will only accelerate the losses and  
15 eliminate the necessary support for high cost areas. While the entrance of  
16 competitors into Embarq’s service territories may serve certain public policy  
17 goals, the Commission must remember that Embarq, unlike its competitors,  
18 provides the public the benefit of being a carrier of last resort with an obligation  
19 to provide service throughout its service area.

1           III.    FUSF IMPUTATION

2    Q.    Sprint-Nextel, in its comments, states that “imputing federal universal service  
3           funds or over earnings in the computation of state earnings will ensure that  
4           the ILECs are not allowed to reap a windfall by double-recovering their costs.”  
5           To what double recovery is Sprint-Nextel referring?

6    A.    It is not clear what Sprint-Nextel means when it refers to a double recovery of  
7           costs and it provides no explanation. It may be that Sprint-Nextel believes that  
8           both the federal high cost loop program and the NUSF allow for full recovery of  
9           the same costs. However, nothing could be further from truth. The total support  
10          received from the two programs is far less than the cost to provide service. For  
11          example, in 2005 United Telephone Company of the West d/b/a Embarq received  
12          \$217,455 in federal high cost loop support for Nebraska. This amount does not  
13          even come close to recovering Embarq’s cost of providing service in Nebraska.  
14          In the same year, Embarq received \$2.4 million of NUSF support, for a combined  
15          total \$2.6 million in high cost loop support. The Commission’s NUSF-26  
16          Distribution Model for Year 1 (which calculated the 2005 support amount)  
17          indicates that Embarq’s total expected support, which is the forward looking  
18          loop cost less expected revenue, is more than \$13.3 million annually. The  
19          amounts Embarq and other companies actually received from the NUSF were  
20          significantly reduced from the expected support levels calculated by the model



1 due to limitations on the fund size. The total amount of federal and state support  
2 Embarq actually received in 2005 recovered less than 20 percent of the total  
3 support the Commission calculated Embarq needed. There is no double  
4 recovery of costs as Sprint-Nextel alleges.

5  
6 **Q. Sprint-Nextel also stated that “federal universal service funds are intended to**  
7 **reduce state costs, and as such should be reflected in the computed state**  
8 **return.” Do you agree with Sprint-Nextel’s statement?**

9 A. I only agree to the extent that the federal *high cost loop* support program is  
10 designed to help offset the cost of the local loop and therefore should be reflected  
11 in the state earnings computation. Embarq and other companies have properly  
12 reflected federal high cost support as intrastate revenue on their NUSF-EARN  
13 forms and that support is included in the state earnings calculation. No other  
14 adjustment for federal universal service support is needed or appropriate. If  
15 anything, the current EARN process is too broad and forces non-supported  
16 services to provide implicit support to basic local service rather than fully  
17 funding the cost of basic local service in high cost areas.

18  
19 **Q. What about support from the other federal USF programs?**

1 A. The other federal universal service programs are not designed to help companies  
2 recover state loop costs. They are designed to recover other costs or lost  
3 revenues, such as interstate access revenue, transport or switching costs. It is  
4 important to note that the NUSF was designed to support only loop costs.  
5 Therefore, it would be inappropriate for the support from federal programs other  
6 than the high cost loop program to be included in the state earnings calculation  
7 for determination of NUSF support. I discussed this issue in my direct  
8 testimony, as did Ms. Sue Vanicek for the Nebraska Rural Independent  
9 Telephone Companies in her testimony.<sup>3</sup>

10  
11 Q. **Sprint-Nextel commented that “[e]xcessive earnings in the federal jurisdiction**  
12 **also are a cost-free source of funds to the ILECs, and should be reflected in**  
13 **their computed earnings on the state side.” Do you agree?**

14 A. No, I do not. As several parties, including Embarq, testified previously the FCC  
15 has created price cap and other incentive plans under which many telephone  
16 companies, including Embarq, operate in the interstate jurisdiction. Under these  
17 incentive plans, companies have the opportunity to control costs and increase  
18 earnings. There is no authorized or guaranteed rate of return for these

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<sup>3</sup> Direct Testimony of Sue Vanicek on behalf of the Rural Independent Companies, pages 5 -7.

1 companies, and therefore no “excessive” earnings to impute to the state  
2 jurisdiction.

3  
4 **IV. URBAN AND RURAL BENCHMARKS**

5 **Q. Several parties, in direct testimony, expressed concern with the proposed**  
6 **urban and rural benchmarks. For instance, Mr. Kevin Kelly, for the Rural**  
7 **Telecommunications Coalition of Nebraska, testified that “charging different**  
8 **local rates for customers of the same small rural LEC (depending on whether**  
9 **the customer resides inside or outside the city limits) will increase**  
10 **administrative costs, result in customer confusion and ultimately create**  
11 **resentment among customers.” Do you agree with Mr. Kelly?**

12 **A.** As I stated in my direct testimony, Embarras believes that the proposed  
13 benchmarks are affordable and can be used to reduce NUSF funding  
14 requirements. Embarras’s concern is not with the proposed benchmarks  
15 themselves, but with the implementation of the separate urban and rural  
16 benchmarks. As Mr. Kelly correctly points out in his direct testimony,  
17 implementing different rates for customers depending on their location within  
18 an exchange will require companies to spend significant amounts of time and  
19 money to upgrade systems. In addition, customers may be confused as to why

1       there are different rates and the applicability of those rates within a single  
2       exchange.

3  
4   **Q.   Mr. Peter Copeland, testifying for Qwest, also expressed some concerns over**  
5       **the different treatment of the two benchmarks in the calculation of NUSF**  
6       **distributions. What is your opinion of the treatment?**

7   **A.   I agree with Mr. Copeland's assessment and my direct testimony discusses the**  
8       **differing treatments. This disparate treatment of the two benchmarks within the**  
9       **distribution mechanism has the effect of disproportionately penalizing**  
10      **companies that have more rural customers. The increase in the rural benchmark**  
11      **should be treated the same within the Support Allocation Methodology ("SAM")**  
12      **model as the increase in the urban benchmark.**

13  
14       **V.    WIRELESS FUND**

15   **Q.   Mr. Kelly stated that "[i]t is crucial that the Commission stabilize the existing**  
16       **NUSF before establishing new programs which will divert the flow of funds**  
17       **required by current recipients." Do you agree?**

18   **A.   Yes, I do. As I stated in my direct testimony, the current proceeding appears to**  
19       **be the result of a customer surcharge that is not bringing in sufficient funds to**  
20       **cover funding obligations as calculated by the existing SAM. In addition to the**

1 many issues surrounding the Commission's proposed changes to the SAM, the  
2 Commission, in the July 18, 2006 staff proposal, proposed reserving \$5 million in  
3 NUSF funding for a program dedicated to wireless infrastructure support. Mr.  
4 Pursley states in his direct testimony that the "\$5 million is reserved for the  
5 dedicated wireless fund pending a Commission decision on how it will establish,  
6 size and disburse support for that purpose. This does not commit the  
7 commission to do anything at this point. Doing so only reserves a certain level of  
8 funding in case the Commission should decide to move forward in NUSF-48."

9  
10 Embarq believes that it is premature to reserve a portion of NUSF funding at this  
11 time for yet another support program. With the financial situation that currently  
12 exists in the NUSF, to reserve such a significant amount of money for a future  
13 program is irresponsible. The Commission should first address current funding  
14 issues before creating a new program.

15  
16 **Q. What is your recommendation for fixing the current funding situation?**

17 **A.** The Commission should immediately increase the surcharge to a level that will  
18 ensure sufficient funding for the existing distributions. The Commission should  
19 then take the time needed to fully examine all of its proposed changes, any  
20 proposed alternative distribution models from other parties, additional funding

1 sources that may be available and finally the impact of those changes and  
2 alternatives on consumers, companies, and the fund before making any  
3 adjustments to the distribution mechanism.

4

5 **Q. Does this conclude your testimony?**

6 **A. Yes.**